Supreme Court, U. S.
FILED
DEC 3 1975
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-596

HOWARD BERSCH,

Petitioner,

v.

ARTHUR ANDERSEN & CO., I.O.S., LTD., and BERNARD CORNFELD,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION FOR I.O.S., LTD. (Now in Liquidation)

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December 3, 1975

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BRIEF IN OPPOSITION FOR I.O.S., LTD.
(Now in Liquidation)

Respondent I.O.S., Ltd. ("IOS"), as now in liquidation pursuant to the Winding-Up Act of Canada, Revised Statutes of Canada, ch. W-10 (1970), prays that this Court deny the Petition for Certiorari herein (the "Petition") for the reasons hereinafter set forth.

Opinions Below

The opinions below, which are attached as Appendices "A" and "B" to the Petition, are officially reported at 519 F.2d 974 (2d Cir. 1975) and 389 F. Supp. 446 (S.D.N.Y. 1974).•

Question Presented for Review

IOS hereby adopts and incorporates by reference as its statement of the Question Presented for Review herein the first "Question Presented" as set forth in the Brief for Arthur Andersen & Co. in Opposition to the Petition (the "Andersen Brief"), at pages 1-2 thereof. It is IOS' position herein that the second "Question Presented" in the Andersen Brief is a subsidiary question fairly comprised in the first Question Presented and need not be stated separately.

Statement of the Case

The basic facts and legal arguments underlying IOS' opposition to the Petition herein are set forth cogently and in considerable detail in the Andersen Brief. Accordingly, IOS will not burden the Court with a repetition of such facts and arguments and they are incorporated by refer-

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• References herein to these opinions will be to the relevant pages of the Federal Reporter or Federal Supplement.

ence herein. IOS will, however, hereinafter set forth certain supplementary facts and arguments and will briefly summarize others which in its view deserve emphasis in opposition to the Petition.

IOS' Liquidation

At the outset, it should be noted that IOS, the company whose common shares were sold in the three stock offerings which are the subject of this action, is now in liquidation proceedings before the courts of New Brunswick, Canada (IOS' corporate domicile) pursuant to the Winding-Up-Act of Canada, Revised Statutes of Canada, 1970, ch. W-10 as amended.

IOS' liquidation proceedings were commenced in August 1973 as a direct result of understandings reached earlier that summer by an international governmental committee (which included representatives of the United States Securities and Exchange Commission) to the effect that—in the aftermath of the now-notorious "Vesco era" in IOS' history—the numerous IOS entities should be wound-up or liquidated in their respective corporate domiciles.* See 519 F.2d at 978 n.4.

IOS has made only a limited and special appearance herein, through its court appointed Co-Liquidators. Said appearance was made solely in an effort to protect the estate of IOS for the benefit of all its worldwide creditors and shareholders, by preventing the decentralized determination of claims against IOS in forums other than the Canadian liquidation court.**

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* The transactions involved in the present action occurred long prior, and are unrelated, to the "Vesco era" which led to IOS' ultimate downfall.

** For these reasons, IOS, as an alternative to its motion to dismiss for lack of subject matter jurisdiction, also moved in the

(*footnote continued on following page*)

Relevant Facts

With respect to the issues raised by the present Petition, the following facts should be emphasized:

—IOS was at the time of the 1969 offerings and at all times thereafter incorporated under the laws of Canada,* with active business offices in Geneva, Switzerland and other locations, all outside the United States. IOS conducted no business in the United States.**

—At no time was IOS stock listed on any United States stock exchange or traded in the securities markets of this country. In fact, in May 1967, IOS had consented to an SEC order which prohibited IOS from engaging in any activity subject to the jurisdiction of the SEC and from making any sales of securities to United States citizens or nationals, except for sales outside the United States to "officers, directors and full time personnel of IOS and its subsidiaries." In connection with the 1969 offerings which are the sub-

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(*footnote continued from preceding page*)

District Court for a stay of proceedings as against it in favor of the Canadian liquidation court. While this stay motion was summarily denied by the District Court, 389 F. Supp. at 463, the Court of Appeals, relying on this Court's decisions in *Canada Southern Ry. Co.* v. *Gebhard*, 109 U.S. 527 (1883) and *Pennsylvania* v. *Williams*, 294 U.S. 176 (1935), granted IOS leave to renew the motion if IOS is not satisfied to proceed with the litigation on the more limited basis resulting from the Court of Appeals' decision. 519 F.2d at 1001. IOS intends to renew its stay motion if the litigation is pursued by petitioner after the Petition is decided.

* Its predecessor company was a Panamanian corporation.

** Although petitioner makes much ado about the American nationality of some of the other participants in the underwritings, the fact is that the "American" companies involved were actually international organizations whose work in connection with the offerings was conducted primarily by or through European offices.

ject of the instant action, IOS was in compliance with the aforesaid order, and at no time since has the SEC taken the position—despite investigation by it—that any part of said offerings violated the 1967 order.

The latter point is not surprising in view of the additional facts that:

—In two of the three offerings involved here, in which more than 7,000,000 shares were sold (*i.e.*, the so-called Drexel and Crang Offerings), *all* of the purchasers were citizens and residents of foreign countries, and not a single share was offered or sold to a citizen or resident of the United States. With respect to the Crang offering it is noteworthy that the prospectus was reviewed and cleared in its initial and final forms by the ten provincial securities commissions of Canada;

—In the third offering, in which 3,950,000 shares were sold (*i.e.*, the IOB Offering), sales were made only to IOS insiders, and all but a small number of such purchasers were citizens and residents of foreign countries;*

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* Actually, only a trivial number—somewhere between 11 and 37—of the purchasers were *resident* Americans; and only some 360 *non-resident* Americans also bought in the IOB offering. Significantly, of the resident American purchasers, at least four of them were also sellers in the IOB Offering. Moreover, of a total of 51,548 IOS shares purchased by resident Americans (out of 11,000,000 in the three offerings), the purchasers of approximately 34,400 such shares were *directors* of IOS—*i.e.*, in substance defendants in this action.

Petitioner Bersch was at the time of his purchase of 600 shares an officer of an IOS-related company which was run by a member of the IOS Board of Directors. For three years prior to his purchase petitioner had been employed by a different IOS-related company. The Court below has raised substantial questions as to whether petitioner or any other similarly situated IOS insider could be considered a proper representative of the class, 519 F.2d at 997-98.

—All sales in all three offerings were consummated in foreign countries;

—The three prospectuses pursuant to which the offerings were made were prepared in foreign countries;

—The only conduct which occurred in the United States in connection with any of the offerings consisted of several preliminary meetings and discussions among representatives of the Drexel Group, Arthur Andersen & Co. and IOS, all of which occurred long before the offerings were made, and none of which involved the formulation of any fraudulent scheme or any contact with the persons who later purchased in any of the offerings. Indeed, the record discloses that the few contacts with the United States related solely to (a) the initial decision of some of the underwriters to participate in one of the offerings (which was itself to be conducted overseas) and (b) several attempts to assure (not avoid) full disclosure in the prospectuses.*

Proceedings Below

In the District Court, all of the defendants herein moved to dismiss the complaint for lack of subject matter jurisdiction, either in its entirety or as to the thousands of non-resident foreign purchasers in the three offerings whom petitioner purported to represent. These motions were denied by the District Court which, however, noted that

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* Interestingly, petitioner has never cited to any United States contact which in any way could be construed as fraudulent or otherwise wrongful. Rather he is reduced to relying on such trivial and insignificant occurrences in the United States as the fact that a certain "sticker", which was affixed to the prospectuses, was drafted in New York (P. 12). Yet the fact is that the "sticker" was designed only to report an SEC investigation of IOS which had been instituted shortly before the prospectuses were distributed. Clearly the addition of the sticker was part of an effort to make full disclosure about IOS—not to conceal or misstate facts.

there was a substantial basis for disagreement with its holding in favor of jurisdiction, and therefore certified the question for immediate appeal pursuant to 28 U.S.C. § 1292(b).

The Court of Appeals reversed the determination that there was subject matter jurisdiction over the claims asserted on behalf of the foreign purchasers. In a lengthy and thoughtful opinion for a unanimous Court, Judge Friendly held that while the domestic conduct of the defendants, even though not fraudulent, might be sufficient to warrant the exercise of jurisdiction over the claims of American purchasers, neither that conduct nor the alleged domestic "effects" of the three offerings could suffice as a basis of jurisdiction over the claims of the thousands of unnamed non-resident foreign purchasers who formed the vast majority of petitioner's class.

Argument

Review by this Court of the Court of Appeals' decision is not warranted. Contrary to petitioner's assertions, the decision of the Court below does *not* raise "important issues with respect to the extraterritorial reach of the federal securities laws" (P. 28-29), but is merely a rebuff—based on a careful study of the facts of this case—of petitioner's attempt to apply the securities laws of the United States to claims asserted on behalf of thousands of unnamed foreign class members based on transactions lacking any significant relationship to the United States.

Unfortunately, petitioner has totally ignored the thrust of the opinion below. The Court of Appeals held that, regardless of the nationality of some of the defendants, foreign nationals residing in foreign countries who purchased securities of a foreign issuer in a foreign country cannot claim a right to sue in a United States court unless the defendants' conduct in the United States was some-

how culpable, wrongful or fraudulent or was otherwise a significant cause of the loss alleged to have been suffered by the foreign purchasers. The Court of Appeals was convinced from the record before it that no such conduct occurred here. That factual determination was crucial to its decision. As such the decision is fully consistent with well-settled principles limiting the extraterritorial reach of American law and thus, under the criteria of Rule 19.1(b) of the Rules of this Court, does not merit consideration here.

I

The Decision Below is Fully Consistent with All Relevant Prior Decisions and with the Statutory Purpose of Section 10(b) of the Securities Exchange Act of 1934

The Court of Appeals' determination that Section 10(b) does not confer federal jurisdiction over securities fraud claims on behalf of foreign purchasers of foreign securities who cannot show that there has been any fraud prepared or practiced in this country is consistent with every relevant prior case. The numerous federal courts which have considered the issue of jurisdiction over foreign transactions involving no domestic fraud have without exception construed Section 10(b) as *not* reaching such extraterritorial transactions. See, *e.g.*, *SEC* v. *Kasser*, 391 F. Supp. 1167, 1176-77 (D.N.J. 1975); *Investment Properties International, Ltd.* v. *I.O.S., Ltd.* [1970-71 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 93,011, at 90,736-37 (S.D.N.Y.), *aff'd without opinion* (unreported 2d Cir. 1971); *Finch* v. *Marathon Securities Corp.*, 316 F. Supp. 1345, 1349 (S.D.N.Y. 1970); see also *Travis* v. *Anthes Imperial Ltd.*, 473 F.2d 515, 526 (8th Cir. 1973); *SEC* v. *United Financial Group*, 474 F.2d 354, 356 (9th Cir. 1973); *Leasco Data Processing Corp.* v. *Maxwell*, 468 F.2d 1326, 1337 (2d Cir. 1968); *Madonick* v. *Denison Mines Ltd.* [1973-

74 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 94,550, at 95,909 (S.D.N.Y. 1974); *Garner* v. *Pearson*, 374 F. Supp. 591, 599 (M.D. Fla. 1974); *Sinva* v. *Merrill Lynch, Pierce, Fenner & Smith*, 48 F.R.D. 385, 386 (S.D.N.Y. 1969); *SEC* v. *Gulf International Finance Corp.*, 223 F. Supp. 987, 994 (S.D. Fla. 1963). The decision below has thus far been followed in the one extraterritorial case reported since the decision was handed down. *F.O.F. Proprietary Funds, Ltd.* v. *Arthur Young & Co.* [Current] CCH Fed. Sec. L. Rep. ¶ 95,286 (S.D.N.Y. 1975).

Petitioner's attempt (P. 24-25) to imply that there is some conflict among the Circuits by reason of the Eighth Circuit's decision in *Travis, supra,* is unavailing. Indeed *Travis,* like each of the other cases cited above, required some evidence of fraudulent conduct in the United States as a pre-condition to finding jurisdiction over an otherwise extraterritorial transaction. Thus, in *Travis* the Court stated: "Here, as in *Leasco,* the scales are tipped in favor of applicability *because misrepresentations were made in the United States.*" 473 F.2d at 526 (emphasis added).*

Moreover the decision of the Court below that jurisdiction does not attach "where the United States activities are merely preparatory or take the form of culpable nonfeasance and are relatively small in comparison to those abroad," 519 F.2d at 987, is entirely consistent with the statutory purpose of Section 10(b). Section 10(b) is an *antifraud statute:* Congress cannot have intended that section to apply to transactions, all indicia of which are otherwise wholly foreign in nature, when it cannot be

* Moreover, the dictum in *Travis* to which petitioner makes reference in the Petition (P. 24-25) cannot under any view be deemed authority for allowing suit by *foreign* purchasers of foreign securities since the plaintiffs in *Travis* were solely *American* shareholders; indeed, the American plaintiffs there had obtained the Canadian securities in suit as consideration for their sale of their controlling interests in an American company to the Canadian defendants.

shown that any fraudulent conduct occurred in the United States—when all that happened here was preliminary and ancillary to the substantial work on the transaction, all performed and consummated overseas. See 519 F.2d at 985 n.24.

It is also indisputable that the fundamental purpose of the American securities laws is the protection of American investors. Accordingly, extraterritorial application of those laws is not justified unless such application would protect American investors. See, *e.g., Leasco Data Processing Corp.* v. *Maxwell, supra,* 468 F.2d at 1336-37; *Schoenbaum* v. *Firstbrook,* 405 F.2d 200, 206, *rev'd in part on other grounds,* 405 F.2d 215 (2d Cir. 1968) (en banc), *cert. denied sub nom. Manley* v. *Schoenbaum,* 395 U.S. 906 (1969); *S.E.C.* v. *Kasser, supra,* 391 F. Supp. at 1175. Here the Court of Appeals has *permitted* all *American* purchasers to sue. The statutory purpose thus is not advanced one iota by also permitting suit by tens of thousands of foreign purchasers.*

Finally, the Court of Appeals was obviously correct in rejecting petitioner's argument that jurisdiction should be assumed because of the alleged domestic "effects" on American securities markets of the 1969 offerings. 519 F.2d at 987-990. Certainly Congress could not have intended the federal courts to take jurisdiction over wholly foreign transactions based merely on highly generalized,

* Of course, as specifically noted by the Court of Appeals, "Congress did not mean the United States to be used as a base for fraudulent securities schemes even when the victims are foreigners, at least in the context of suits by the SEC or by named foreign plaintiffs," 519 F.2d at 987, and that Court upheld jurisdiction where the United States had been used as a base for such a scheme in *IIT* v. *Vencap, Ltd.,* 519 F.2d 1001 (2d Cir. 1975), decided the same day as this case. But the distinction drawn by the Court between the fraudulent domestic conduct found in *Vencap* and the wholly preliminary, non-fraudulent conduct found in the present case is fundamental and obviously consistent with the basic purposes of the antifraud statute.

speculative and self-serving claims that foreign investor confidence and trust in the American market was impaired. Yet such self-serving claims are all that petitioner has offered in support of his "effects" argument.

The whole of petitioner's proof of these "effects" was a brief affidavit by one Associate Professor Morris Mendelson, prepared at petitioner's instance. Indeed, as a close reading of that document discloses, even Professor Mendelson recognizes that the alleged loss of investor confidence which his affidavit describes stemmed not from the 1969 offerings but rather from IOS's financial collapse—which did not even begin until perhaps April of 1970, more than six months *after* the 1969 offerings were consummated. Any effects traceable to those events—or to the events following thereafter, when IOS fell into the hands of Robert L. Vesco and his associates—are completely irrelevant to the issue of jurisdiction over the 1969 offerings. Indeed even the District Court—which upheld jurisdiction over the foreign purchasers' claims—stated with respect to petitioner's "effects" argument that, notwithstanding the Mendelson affidavit, "the impact on the American securities market of the I.O.S. offering [*sic*] was in fact less than direct." 389 F. Supp. at 461. This conclusion is substantiated by a major SEC report to Congress in 1971 which concluded that the sales by IOS-related mutual funds had no "significant direct effect on general market stability". *Institutional Investor Study Report,* H.R. Doc. No. 64, 92nd Cong., 1st Sess., vol. 3, p. 947 (1971).

In this connection it is further highly noteworthy that the SEC, which is charged by the Exchange Act with protecting the integrity of the United States securities markets, has not supported petitioner's position herein by deed or word. Indeed, contrary to petitioner's elaborate argument that the SEC's posture in matters of the kind involved here would be in favor of jurisdiction in United States courts, the facts are that (a) the Commission never took any action against the participants in the 1969 offer-

ings based on any aspect of their participation therein—notwithstanding that IOS furnished complete information about the offerings to the Commission, *cf.* 519 F.2d at 991; (b) prior to IOS' liquidation the SEC *had* instituted a major court proceeding based on later events during the "Vesco era" in IOS' history* and said nothing about the 1969 offerings; and (c) the SEC did not even file a brief *amicus curiae* in support of petitioner's position below, notwithstanding that it did so in *IIT* v. *Vencap, Ltd., supra,* which involved the issue of jurisdiction over extraterritorial transactions where fraud *had* been practised in this country. See p. 9, n.*, *supra.***

II

Compelling Reasons of Policy Also Support the Decision Below

Compelling reasons of policy—all of them illustrated by the facts of this very case—also support the decision below declining jurisdiction over the foreign purchasers' claims.

Thus this Court and the lower federal courts have long recognized that unwarranted intrusion into foreign transactions by the courts of the United States creates the risk of conflict with the legal systems of friendly sister nations and therefore should be avoided. See, *e.g., Scherk*

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* *S.E.C.* v. *Vesco,* 72 Civ. 5001 (S.D.N.Y.) (C.E.S.).

** Moreover, it is significant that the SEC has expressly exempted foreign offerings from the registration requirements of the Securities Act—even when the issuer, unlike IOS, is an American company. This exemption is available without regard to "whether the offering originates from within or outside of the United States, whether domestic or foreign broker-dealers are involved and whether the actual mechanics of the distribution are effected within the United States, so long as the offering is made under circumstances reasonably designed to preclude distribution or redistribution of the securities within, or to nationals of, the United States." S.E.C. Release No. 33-4708 and No. 34-7366, 17 C.F.R. § 231.4708, 1 CCH Fed. Sec. L. Rep. ¶ 1362 (1964). There can be no question that the 1969 offerings—even if they had been made by an *American* issuer—would have satisfied these guidelines.

v. *Alberto-Culver Co.*, 417 U.S. 506, 517 & n.11 (1974); *Foley Bros.* v. *Filardo*, 336 U.S. 281, 285 (1949); *Investment Properties International, Ltd.* v. *I.O.S., Ltd., supra* [1970-71 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 93,011, at 90,735.

In this case, the prospect of such conflict is a near-certainty if the decision of the Court of Appeals is reversed. Thus, undisputed affidavits of foreign law submitted below establish that the courts of England, the Federal Republic of Germany, Switzerland, Italy and France would not recognize a judgment in this case in favor of the defendants as a bar to an action by their own citizens in their own countries. 519 F.2d at 996-97. Moreover, hundreds of claims by purchasers in the 1969 offerings—all members of petitioner's alleged class—have already been asserted, and some of them adjudicated, in Swiss proceedings against respondent Bernard Cornfeld.

With reference to IOS in particular, by virtue of its ongoing liquidation in the Canadian courts, there is obviously a strong interest in assuring that claims against the estate are asserted in those centralized proceedings. See *Canada Southern Ry. Co.* v. *Gebhard, supra; Pennsylvania* v. *Williams, supra.* At the very least, difficult questions of recognition of foreign judgments will arise in those proceedings if this action goes forward against IOS in the courts of the United States.

Moreover considerations of sound judicial administration strongly support the Court of Appeals' decision. As stated by that Court:

> When as here, a court is confronted with transactions that on any view are predominantly foreign, it must seek to determine whether Congress would have wished the precious resources of United States courts and law enforcement agencies to be devoted to them rather than leave the problem to foreign countries.
>
> —519 F.2d at 985.

Here it is crystal clear that adjudication of the foreign purchasers' claims in the federal courts would be extraordinarily difficult, if not impossible. The management of a class action where virtually the entire class resides in foreign countries all over the world would impose enormous burdens on already overtaxed district courts, and it is hard to see how compliance with the various protections embodied in Rule 23 of the Federal Rules of Civil Procedure could be assured. Compare 519 F.2d at 996 & n.47; *cf. id.* at 997 n.48. Furthermore, as noted above, there are very serious doubts whether any adjudication in our courts would be given effect by foreign courts.

For these reasons of comity and sound judicial administration as well, the Court of Appeals was correct in holding that the claims asserted on behalf of the foreign purchasers should be dismissed.

CONCLUSION

The Petition for Certiorari should be denied.

December 3, 1975.

Respectfully submitted,

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